BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALL

01-18-08 04:59 PM

Order Instituting Investigation to Consider Policies to
Achieve the Commission's Conservation Objectives for
Class A Water Utilities.

In the Matter of the Application of Golden State Water Company (U 133 E) for Authority to Implement Changes in Ratesetting Mechanisms and Reallocation of Rates.

Application of California Water Service Company (U 60 W), a California Corporation, requesting an order from the California Public Utilities Commission Authorizing Applicant to Establish a Water Revenue Balancing Account, a Conservation Memorandum Account, and Implement Increasing Block Rates.

Application of Park Water Company (U 314 W) for Authority to Implement a Water Revenue Adjustment Mechanism, Increasing Block Rate Design and a Conservation Memorandum Account.

Application of Suburban Water Systems (U 339 W) for Authorization to Implement a Low Income Assistance Program, an Increasing Block Rate Design, and a Water Revenue Adjustment Mechanism.

Application of San Jose Water Company (U 168W) For an Order Approving its Proposal to Implement The Objectives of the Water Action Plan Investigation 07-01-022 (Filed January 11, 2007)

Application 06-09-006 (Filed September 6, 2006)

Application 06-10-026 (Filed October 23, 2006)

Application 06-11-009 (Filed November 20, 2006)

Application 06-11-010 (Filed November 22, 2006)

Application 07-03-019 (Filed March 19, 20007)

REPLY COMMENTS OF SAN JOSE WATER COMPANY AND THE DIVISION OF RATEPAYER ADVOCATES TO COMMENTS ON SETTLEMENT AGREEMENT

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I. INTRODUCTION

Pursuant to Rule 12.2 of the Commission's Rules of Practice and Procedure (Rules), San Jose Water Company (SJWC or San Jose) and the Division of Ratepayer Advocates (DRA) (jointly, the Parties) submit these Reply Comments on the Settlement Agreement between the Division of Ratepayer Advocates and San Jose Water Company on Conservation Rate Design Issues (Settlement)¹ in response to other parties' Comments on the Settlement.

On December 13, 2007, Consumer Federation of California (CFC) filed comments on the Settlement challenging the appropriateness of the proposed conservation rates and purporting to propose an alternate rate design.² As will be shown below, CFC's alternate rate design has numerous errors and is therefore unusable.

On December 14, 2007, the National Consumer Law Center (NCLC), The Utility Reform Network (TURN), Latino Issues Forum (LIF), and Disability Rights Advocates (collectively referred to as Joint Consumers) filed comments that recommended modifications to the Settlement relating to public education/outreach and data collection for monitoring purposes. The Joint Consumers, however, do not appear to actively oppose the Settlement.³

II. REPLY TO THE JOINT CONSUMERS' COMMENTS

The Joint Consumers believe that an aggressive notice and outreach campaign is necessary to ensure that San Jose's customers understand the changes to their bill, the

¹ Settlement Agreement between the Division of Ratepayer Advocates and San Jose Water Company on Conservation Rate Design Issues (November 14, 2007) (Settlement), filed as an attachment to the Motion of the Division of Ratepayer Advocates and San Jose Water Company To Approve Settlement Agreement (Settlement Agreement Attached) (November 14, 2007) (11/14/07 Motion).

² The Consumer Federation of California's Comments on the Settlement Agreement Between the Division of Ratepayer Advocates and San Jose Water Company on WRAM and Conservation Rate Design Issues (December 13, 2007) (CFC's Comments).

³ Comments of the National Consumer Law Center, The Utility Reform Network, Latino Issues Forum and Disability Rights Advocates on the Conservation Rate Design Settlement of the Division of Ratepayer Advocates and San Jose Water Company (December 14, 2007) (Joint Consumers' Comments).

reason for the changes, and how the new bill amounts are calculated.⁴ Joint Consumers also believe that in order to gauge the effect of the proposed conservation rates on residential consumers, and the impact on low-income consumers in particular, certain data points and reports are crucial.⁵

San Jose and the Joint Consumers have been engaged in productive settlement negotiations and SJWC represents that the parties are currently finalizing an agreement in principle on collection of data points, reporting schedules, consumer outreach and education issues. SJWC expects to be submitting a settlement with the Joint Consumers reflecting such agreement in principle within the next few weeks.

III. REPLY TO CFC'S COMMENTS

The arguments of CFC are similar to those presented by CFC in opposition to the proposed conservation rate design settlements for California Water Service Company (CWS), Golden State Water Company (GSWC), Park Water Company (Park), and Suburban Water Systems (Suburban). CFC urges that the San Jose Settlement "be rejected and conservation rates set in the manner recommended in the testimony and exhibits of CFC's witness offered in the Phase 1A hearing and as more fully described herein."

⁴ Joint Consumers' Comments at 3.

 $[\]frac{5}{2}$ *Id.* at 6.

⁶ The Consumer Federation of California's Comments on Settlement Agreement Between DRA, TURN and Cal Water Service Company (June 27, 2007).

² The Consumer Federation of California's Comments on Settlement Agreement Between the Division of Ratepayer Advocates and Golden State Water Company on WRAM and Conservation Rate Design (November 19, 2007).

⁸ The Consumer Federation of California's Comments on Settlement Agreement Between DRA and Park Water Company (June 27, 2007).

⁹ The Consumer Federation of California's Comments on Settlement Agreements Between the Division of Ratepayer Advocates and Suburban Water Systems (May 23, 2007).

¹⁰ CFC's Comments at 25.

However, a recently issued Proposed Decision for Phase 1A (PD) has proposed adopting the CWS settlement, in part, and the Park and Suburban settlements in full. While the PD carefully considers the testimony and exhibits that CFC proffered in that phase, it does not modify a settlement based on CFC's arguments. The Parties recognize that that a PD cannot be cited for the purpose of establishing a precedent for the San Jose Settlement; however, it is useful to be mindful of the PD as an insight into how the Commission has addressed the concerns raised by CFC in an earlier phase of this proceeding.

CFC's Comments misunderstand the proposed settlement submitted by the Parties. Instead, the Comments continue to push for aggressive conservation rate designs that are **not** in the public interest in this first step of price-related conservation efforts in San Jose's service territory. In addition, while CFC's Comments on the Settlement between DRA and San Jose appear, for the first time, to offer "alternative rate proposals," the proposals have serious flaws in many ways as discussed herein. Finally, CFC does not identify any contested issues of material fact that merit an evidentiary hearing on the Settlement. Thus, while CFC, the Parties, and the Commission may share the same long-term conservation goals, the Parties urge the Commission to deny CFC's request for an evidentiary hearing on the Settlement, and allow San Jose to begin phasing in the appropriate pricing signals as proposed in the Settlement.

A. No Cost Allocation Study is Necessary.

CFC argues that the Parties developed proposed rates without first determining how San Jose's cost of service should be allocated to each customer class, ¹² and that "[t]he Settlement cannot be found reasonable without evidence that costs are being fairly

¹¹ Proposed Decision of ALJ Grau (mailed January 15, 2008). The PD would not adopt the proposed non-residential rate design for CWS on the grounds that the current record does not provide sufficient justification for the proposed rates, but does not appear to rely on CFC's superficial criticisms of CWS' non-residential rate design. PD at 16-18; *see also* CFC Comments on CWS Settlement at 19-21.

 $[\]frac{12}{12}$ CFC's Comments at 5, 6-9.

allocated between customer classes." CFC's argument demonstrates a misunderstanding of the purpose of the proposed settlement. The rates proposed in the Settlement maintain the existing allocation of costs between San Jose's customer classes, as previously approved by the Commission. Thus, far from having "admitted" that "[n]o cost allocation studies were used to develop rates in the proposed settlement," the Parties properly designed rates based on the cost allocation adopted by the Commission in SJWC's last general rate case decision, an allocation that is presumptively reasonable. The Commission should reject CFC's cost allocation arguments as being beyond the scope of San Jose's Application and this Settlement.

B. It Is Reasonable that the Trial Program Not Include Changes to Non-Residential Rates.

CFC claims that the Parties have failed to justify the lack of conservation rates for non-residential customers. As the Parties indicated in the Motion to approve the Settlement Agreement, the Parties did not propose tiered quantity rates for non-residential customer classes because approximately 81% of the total revenue from these customer classes already is collected through the volumetric (or quantity) rate in accordance with the conservation guidelines. DRA and SJWC believe that their proposed rate design in the Settlement Agreement meets the intent of BMP 11. CFC, on the other hand, effectively dismisses BMP 11.

More specifically, under the existing rate design San Jose recovers approximately 69.2% of its residential revenue and 80.93% of its non-residential revenue through volumetric rates. Combining all customer classes, San Jose recovers approximately 73.4% of its revenue through volumetric rates and 26.6% of its revenue through meter charges. The California Urban Water Conservation Council (CUWCC) recommends in

 $[\]frac{13}{2}$ CFC's Comments at 9.

¹⁴ CFC's Comments at 7.

¹⁵ D.06-11-015.

 $[\]frac{16}{10}$ CFC's Comments at 9-10.

Best Management Practices 11 (BMP 11) that a water utility should recover at least 70% of revenues through volumetric rates to be consistent with conservation-oriented pricing. Therefore, San Jose's existing rates for non-residential customers are already considered conservation rates.

Additionally, the AWWA acknowledges that:

...it is more difficult to set fair quantity limits for commercial and industrial customers than for residential customers. Non-residential customers typically do not exhibit homogeneous usage patterns. Because of the extreme diversity in the numbers, types, and sizes of commercial and industrial customers, specific quantity targets or rate limits are unreasonable for large number of these customers. 17

Furthermore, the Suburban settlement under consideration in Phase 1A does not include conservation rates for non-residential customers, while the Park settlement only reduces the meter charge for non-residential customers to a level that complies with BMP 11. The recently issued PD would approve the Suburban and Park settlements despite their lack of tiered conservation rates, suggesting that it is unlikely that the Commission would now impose such a requirement on SJWC. 19

C. CFC Has A Flawed Understanding Of How The Settlement's Consumption Breakpoints Were Set.

CFC alleges that "[t]he tiered rates proposed for residential customers are not designed in the way the parties have described them in the Settlement." CFC appears to misunderstand how the Parties developed the consumption breakpoints for the two tiers proposed in the Settlement.

¹⁷ Principles of Water Rates, Fees and Charges, American Water Works Association Manual M1, Fifth Edition (2000) (AWWA Manual M1) at 166.

¹⁸ PD at 20-23.

<u>19</u> *Id*.

 $[\]frac{20}{20}$ CFC's Comments at 5; see also id. at 10-12.

For example, CFC cites paragraph V.A.2.a of the Settlement²¹ and erroneously concludes that "the parties agreed that the breakpoint should be set at 'average monthly consumption during the winter months as a proxy for indoor water usage." In fact, the language cited by CFC does not identify a breakpoint, but merely states that the Parties identified three winter months and calculated the average consumption across those months to develop a proxy for indoor water usage. The consumption breakpoints themselves are described in paragraph V.D.1 of the Settlement.²³

Similarly, CFC argues that "there is no instance where the breakpoints used to fix rates constitutes the mid-point between average monthly and annual winter uses, if data developed for customers with different size meters is examined." This statement is also factually incorrect. For example, the chart set forth below shows instances where the method was used.

Meter Size	No. of Customers	% of Customers	Avg Monthly Use	Avg Winte r use	Calculated Midpoint between	Rounded up to nearest integer	Rounded down to nearest integer	Assigned Breakpoint
5/8-inch	830	0.4%	14.5	10.2	12.4	13	12	13
3/4-inch	171,333	86.7%	14	10.2	12.1	13	12	13
1-inch	23,159	11.7%	20.7	10.2	15.5	16	15	13
1-1/2-inch	1,775	0.9%	42.5	10.2	26.4	27	26	26
2-inch	439	0.2%	77.8	10.2	44.0	44	44	26
Sum	197,536							

For the 1-inch and the 2-inch meters, the Parties made a judgment call and included them at breakpoints of 13 and 26, respectively. The Parties based the design on the meters sized at ¾ inch because 86.7% of the customers had that type of meter. The

²¹ Settlement at 5.

²² CFC's Comments at 10.

²³ Settlement at 6-7. The Settlement describes that there is a breakpoint creating two consumption blocks for each meter size, and the breakpoints are calculated using certain meter-specific average consumption levels. *Id.*

²⁴ CFC's Comments at 12.

Parties also used 10.2 ccf as average winter use for all customers because SJWC did not keep separate data that showed winter use by meter size.

For the larger meters, the Parties used a breakpoint at 26 ccf, which was based on the recorded data for 1.5-inch meters. More than 80% of the customers in this group have 1.5-inch meters.

D. A Phased-In Conservation Rate Design Is Appropriate For San Jose.

The Parties' main goals in designing conservation rates were both to prevent rate shock as well as any adverse impact on the financial viability of SJWC. San Jose's take or pay provisions in its contract with the Santa Clara Valley Water District ultimately limits the conservation outcomes that are reasonable and effective. The program proposed by DRA and SJWC is a pilot program that will evolve over time. If it is determined with time and experience that a third tier is needed to send stronger conservation signals, changes can be evaluated in the GRC process.

Guidelines from the California Urban Water Conservation Council (CUWCC) guidelines suggest that:

The principal objective of phase-in plans is to avoid "rate shock" – a sharp pain experienced by customers facing a very large increase in their water bill. Water customers benefit from phase-in plans because a sharp increase for a vital utility service is avoided. Phase-in plans do not, in the long-term, eliminate the need for rate hikes; they merely spread increases out over a longer period of time, thus cushioning the impact of rising costs on ratepayers. ²⁵

In addition, rate design experts advise that:

...the initial differential in the level of the peak period rate should be relatively modest as compared with the off peak rates in order to allow time to change behavior and

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²⁵ Designing, Evaluating and Implementing Conservation Rate Structures, A Handbook Sponsored by the California Urban Water Conservation Council (July 1997) at 9-4.

consumption patterns. The price differential between demand periods can be gradually increased over time, if appropriate. ²⁶ DRA and SJWC followed these rate design principles in the Settlement.

Further, not only do the Parties believe that a gradual phase-in approach to conservation rates is appropriate here, so does the Proposed Decision in Phase IA. The PD finds that to adopt conservation rates outside of a rate case, "a realistic target for the conservation rate designs adopted should be a 0.5% - 1% reduction in consumption per year for each year or partial year the program is in place prior to the utility's next rate case." The same standard should apply to San Jose as well.

In Section IV of the Settlement, the Parties acknowledge that this is a Trial Program, and that it will be reviewed in San Jose's next general rate case.²⁸ The Parties also agree that if the proposed Trial Program results in a disparate impact on ratepayers or shareholders, the Parties will meet to discuss adjustments to the proposed Trial Program.²⁹ The Parties expect that, over time, the Trial Program will be refined based upon lessons learned and additional data collected.

E. CFC's Proposed Rate Designs Have Serious Flaws.

In comparison to CFC's previous criticisms of the conservation rate design settlements that have been filed in this proceeding, CFC's Comments on the San Jose Settlement appears to offer an alternative rate design. CFC first states that it "has developed a tiered rate structure to demonstrate that conservation rates can be designed to target large residential users of water,"³⁰ but later appears to offer a three tier rate design as actual "alternative" rates.³¹ CFC also provides a four-tiered rate design "for illustrative"

²⁶ AWWA Manual M1 at 104.

²⁷ PD at 11.

²⁸ Settlement at 5.

²⁹ Id.

 $[\]frac{30}{2}$ CFC's Comments at 5 (emphasis added).

 $[\]frac{31}{2}$ CFC's Comments at 20-21.

purposes."32 While CFC and the Parties share the same long-term goal of utilizing price signals to effectuate conservation, as described more fully below, both of CFC's proposals have significant flaws that render them inoperable as actual "rate design alternatives."

The following table is based on the data from CFC's proposed three tier rate design:

CFC's PROPOSED 3 TIER RATE DESIGN

	Tier Consum- ption (ccf)	Proposed Rates	% of customers	sales in tier (Ccf)	Revenue(\$) in tier	% revenue	% consum- ption
Tier 1	<10	\$1.90	45.19%	6,256,663	11,890,700	9.32%	17.61%
Tier 2	10-20	\$2.60	32.71%	11,266,688	29,289,558	22.96%	31.72%
Tier 3	>20	\$4.80	22.10%	17,999,902	86,400,250	67.72%	51%
			100.00%	35,523,253	127,580,508	100.00%	100.00%

CFC's alternate three tier rate design raises the following issues:

- CFC's proposed design increases the bills of large users (>100 ccf) by over 90%, which would result in *de facto* rate shock. $\frac{33}{2}$
- CFC's proposed design more than doubles the bills of the largest users (>140 ccf), regardless of meter size. This adversely impacts ratepayers who have larger meters, who might potentially consume more water simply because of a larger meter size, and who might not have control over their consumption. Also the largest Residential customers are likely to be multi-family units and apartment complexes that may have low-income customers behind the meter. Thus, such a severe rate design could adversely impact water users that could least afford it.
- CFC's proposed design charges customers consuming in the third tier (22.1% of customers), 67.7% of revenues. This design places a large percentage of SJWC's revenue at risk.

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³² CFC's Comments at 21-22.

³³ See the bill impact analysis in the Attachment at pages 2 and 4.

 $[\]frac{34}{}$ Id.

- In fact the revenues from the third tier would collect \$86,400,250, i.e. more than SJWC's entire quantity revenue requirement of \$77,085,459.
- CFC's proposed 3-tier design is not revenue neutral and would overcharge ratepayers by \$50,495,049 or 65.5% more than the quantity revenue target of \$77,085,459.

The following table is based on the data from CFC's proposed four tier rate design:

CFC's PROPOSED 4 TIER RATE DESIGN

	Tier Consum- ption (ccf)	Proposed Rates	% of customers	sales in tier(Ccf)	Revenue(\$) in tier	% revenue	% consum- ption
Tier 1	<10	1.800	45.19%	6,256,663	11,262,087	9.05%	17.61%
Tier 2	10-20	2.500	32.71%	11,266,688	28,164,917	22.64%	31.72%
Tier 3	20-40	3.700	17.81%	7,496,524	27,736,014	22.29%	21.10%
	>40	5.450	4.29%	10,503,378	57,242,937	46.01%	29.57%
			100.00%	35,523,253	124,405,956	100.00%	100.00%

CFC's alternate four tier rate design raises the following issues:

- CFC's proposed design increases the bills of large users (>95 ccf) by over 90%, which would result in *de facto* rate shock. 35
- CFC's proposed design more than doubles the bills of the largest users (>115 ccf), regardless of meter size. 36 This adversely impacts ratepayers who have larger meters, who might potentially consume more water simply because of a larger meter size, and who might not have control over their consumption. Also the largest Residential customers are likely to be multi-family units and apartment complexes that may have low-income customers behind the meter. Thus, such a severe rate design could adversely impact water users that could least afford it.
- CFC's proposed design charges customers consuming in the proposed tiers 3 and 4 (22.1% of customers), 68.3% of revenue. This design places a large percentage of San Jose Water Company's revenue at risk.

 $[\]frac{35}{2}$ See the bill impact analysis in the Attachment at pages 6 and 8...

³⁶ Id.

• In fact, the revenues from the third and fourth tiers would collect \$84,978,952, i.e. more than SJWC's entire quantity revenue requirement of \$77,085,459.

• CFC's proposed 4 tier design is not revenue neutral and would overcharge ratepayers \$ 47,320,497 i.e. 61.4% more than the quantity revenue target of \$77,085,459.

For the above reasons, CFC's proposed three and four tier rate designs are clearly not in the public interest and certainly are not viable, and therefore should be rejected.

IV. CONCLUSION

In summary, the Commission should reserve decision on the comments filed by the Joint Consumers, to allow San Jose and the Joint Consumers to complete an agreement on collection of data points, reporting schedules, consumer outreach and education issues that will soon be submitted to the Commission for approval. Furthermore, the Commission should dismiss CFC's criticisms of the Settlement as lacking in merit, conclude that no party has presented contested issues of material fact that warrant evidentiary hearings, and approve the Trial Program set forth therein as a solid first step towards the design and implementation of an effective conservation rate program for San Jose's customers.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that I have this day served a copy of "REPLY COMMENTS OF SAN JOSE WATER COMPANY AND THE DIVISION OF RATEPAYER ADVOCATES TO COMMENTS ON SETTLEMENT AGREEMENT" in I.07-01-022 et al. by using the following service:

[X] E-Mail Service: sending the entire document as an attachment to all known parties of record who provided electronic mail addresses.

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Executed on January 18, 2008 at San Francisco, California.

/s/ Joanne Lark

Joanne Lark

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Service List I.07-01-022 et al.

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